

**Internal Revenue Service**  
Appeals Office

**Department of the Treasury**

**Taxpayer Identification Number:**

Release Number: **201217028**  
Release Date: 4/27/2012  
Date: February 1, 2012

**Person to Contact:**

Tel:  
Fax:

**Tax Period(s) Ended:**

**UIL: 501.03-05**

**Certified Mail**

:

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code (the "Code"). It is determined that you do not qualify as exempt from Federal income tax under section 501(c)(3) of the Code effective

The revocation of your exempt status was made for the following reason(s):

You have not demonstrated that you are operated exclusively for exempt purposes within the meaning of Internal Revenue Code section 501(c)(3) and Treasury Regulations section 1.501(c)(3)-1(d). You did not engage primarily in activities that accomplish one or more exempt purposes specified in section 501(c)(3). You are operated for a substantial non-exempt purpose, which is not an exempt purpose. You are operated for the benefit of private rather than public interests and your activities resulted in substantial private benefit. Further, your net earnings inured to the benefit of private shareholders or individuals.

Contributions to your organization are not deductible under section 170 of the Code.

You are required to file Federal income tax returns on Forms 1120 for the tax periods stated in the heading of this letter and for all tax years thereafter. File your return with the appropriate Internal Revenue Service Center per the instructions of the return. For further instructions, forms, and information please visit [www.irs.gov](http://www.irs.gov).

If you were a private foundation as of the effective date of revocation, you are considered to be taxable private foundation until you terminate your private foundation status under section 507 of the Code. In addition to your income tax return, you must also continue to file Form 990-PF by the 15th Day of the fifth month after the end of your annual accounting period.

Processing of income tax returns and assessments of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Code.

If you decide to contest this determination, you may file an action for declaratory judgment under the provisions of section 7428 of the Code in one of the following three venues: 1) United States Tax Court, 2) the United States Court of Federal Claims, or 3) the United States District Court for the District of Columbia. A petition or complaint in one of these three courts must be filed within 90 days from the date this determination letter was mailed to you. Please contact the clerk of the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217. See also Publication 892.

You also have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have

to file a petition in a United States Court. The Taxpayer Advocate can however, see that a tax matters that may not have been resolved through normal channels get prompt and proper handling. If you want Taxpayer Advocate assistance, please contact the Taxpayer Advocate for the IRS office that issued this letter. You may call toll-free, 1-877-777-4778, for the Taxpayer Advocate or visit [www.irs.gov/advocate](http://www.irs.gov/advocate) for more information.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely Yours,

Appeals Team Manager

Enclosure: Publication 892

cc:



**DEPARTMENT OF THE TREASURY**

Internal Revenue Service  
WASHINGTON, DC 20224

**TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION**

**Date:** October 31, 2005

**Taxpayer Identification Number:**

**Form:**

**Tax Year(s) Ended:**

**Person to Contact: / ID Number:**

**Contact Number:**

Telephone:

Fax:

**Certified Mail – Return Receipt Requested**

Dear Mr. ,

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us, a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals Office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

IRS

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Director, EO Examinations

**ENCLOSURES:**

Publication 892

Publication 3498

Report of Examination: Form 4621, Form 886-A, Form 6018

cc: George Constantine, Esq., Power of Attorney

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer:</b> XXXXX		<b>Tax Year(s) Ended:</b> December 31, XXXX

**ISSUES:**

1. Whether XXXXX (XXX) has operated exclusively for exempt purposes within the meaning of Section 501(c)(3) of the Internal Revenue Code if:
  - a. It is engaged primarily in activities that accomplish, more than insubstantially, a nonexempt purpose; or
  - b. Part of its net earnings inured to the benefit of any private shareholder or individual; or
  - c. Its operations confer, more than incidentally, a private benefit to selected individuals rather than for the benefit of the public's interest?

**This Section Intentionally left Blank**

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer:</b>  XXXXX		<b>Tax Year(s) Ended:</b>  December 31, XXXX

**FACTS:**

**1. BACKGROUND**

An audit of XXXXX (hereinafter XXX) was conducted for the tax year ending December 31, XXXX.

**a. Formation**

XXX was incorporated as "XXXXX, Inc." under the laws of the State of XXXXX as a non-stock, nonprofit corporation on August 15, XXXX. The initial articles of incorporation state that the purpose for which XXX is organized is "to provide credit counseling services to the public."

**b. Incorporator and Initial Directors**

The Articles of Incorporation identifies Mr. XXXXX, as XXX's incorporator, but do not disclose the names of any officer or director. Mr. XXXXX also acted as XXX's initial registered agent.

On October 31, XXXX, M. XXXXX elected the following individuals to serve as XXX's initial directors:

- XXXXX
- XXXXX
- XXXXX

**c. Governance**

By-laws were adopted on November 1, XXXX by XXX, XXX and XXX. No amendments to the By-laws have been evidenced.

Article III of the By-Laws, states the board of directors shall manage the business and property of XXX. This Article also provides that the board shall be comprised on no fewer than three directors, elected annually for a one year term or until the next annual meeting and the election and qualification of their successors.

Under Article IV, the officers shall include a President, Secretary and Treasurer. All officers are elected for a one year term and shall hold office until their successors are elected and qualified by the board of directors. The board also may elect other officers, assistant officers and agents it deems necessary.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	Schedule or Exhibit No.
Name of Taxpayer:  XXXXX		Tax Year(s) Ended:  December 31, XXXX

The specific duties and responsibilities of each office are described as follows:

The President shall serve as chief executive officer; shall preside over meetings; shall have general supervision of the affairs of XXX; shall sign or countersign all certificates, contracts and other instruments of XXX, as authorized by the board; shall make reports to the board; and shall perform all such other duties as are incident to his office or are properly required of him by the board.

The Secretary shall issue calls and/or notices for all meetings; shall keep minutes; shall have charge of the seal and the books of XXX; shall sign with the president and/or affix the seal to such instruments that require such seal or signature; and shall perform such other duties as are incident to his office or are properly required of him by the board.

The Treasurer shall have custody of all monies and securities; shall keep regular books of account; shall sign or countersign such instruments as required; and shall perform such other duties as are incident to his office or are properly required of him by the board.

With respect to executive compensation, the board of directors shall have the power to fix the compensation of officers, assistant officers and agents.

Article VIII permits related party transactions between (1) XXX and one or more of its directors or officers, or (2) between XXX and any other corporation, partnership, association or other organization in which one or more of its directors or officers have a financial interest as long as such transactions are (1) disclosed or are known to all directors voting on the matter and (2) authorized, approved or ratified by vote or by written consent, excluding the vote of the interested party.

## **2. APPLICATION FOR RECOGNITION OF TAX EXEMPT STATUS**

A Form 1023, Application for Recognition of Exemption under Section 501(c)(3) of the Internal Revenue Code (Application), was filed with the Internal Revenue Service (Service) on October 19, XXXX. The application was submitted under the penalties of perjury by XXXXX, President (hereinafter XXX). The other members of the organization's governing body were listed as: XXXXX (hereinafter XXX) - Director, XXXXX (hereinafter XXX) - Director.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer:</b>  XXXXX		<b>Tax Year(s) Ended:</b>  December 31, XXXX

XXX's, resume states that he is a XXXX graduate of XXXXX High School in XXXXX, XXXXX.

He identifies himself as the owner and operator of XXX. XXX is also the founder, President and sole shareholder of XXXXX, XXXXX, Corporation (hereinafter XXXXX) and XXXXX, Inc. (hereinafter XXXXX), both are for-profit corporations organized in the State of XXXXX. Prior to XXX, XXX's prior work experience included counseling consumers about the advantages of bi-weekly mortgage plans for XXXXX.

He also has owned and operated the following businesses:

- (1) XXXXX, Inc., XXXX-XXXX, a wholesale manufacturer and distributor of children's clothing;
- (2) XXXXX, XXXX-XXXX, an art and framing distribution company; and
- (3) XXXXX., XXXX-XXXX, comprised of four art galleries.

Director XXX's resume states she is a XXXX graduate of XXXXX High School in XXXXX, XXXXX. After graduating from high school, XXX was employed by a clothing store taking credit applications and checking credit references. Later on, XXX owned and operated a department store from XXXX to XXXX and a rare coin store, from XXXX-XXXX. In XXXX, XXX retired and moved to the State of XXXXX. After completing her service to XXX, XXX founded XXXXX, Inc. in XXXX, where she was President, Treasurer and director.

Director XXX's resume states she graduated from XXXXX High School in XXXX and was a housewife until she began working with XXX at XXXXX and XXXXX, Inc. Prior to her election as director, XXX was employed at XXXXX where she performed bookkeeping functions and credit verifications. She is also the mother of XXX.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer:</b> XXXXX		<b>Tax Year(s) Ended:</b> December 31, XXXX

**a. Description of Activities and Operations**

In response to Part II, Item 1 of the Application, XXX stated that it provides the following services to its clients:

- ▲ credit rebuilding service, which involves the removal of negative inaccurate information on client's credit reports;
- ▲ informing clients of their legal rights under the Fair Debt Collection Act;
- ▲ debt consolidation, which involves
  - (1) dealing with clients that are behind on their bills;
  - (2) negotiating with their creditors to
    - (i) reduce their payments;
    - (ii) reduce or eliminate interest charges; and
    - (iii) re-age their accounts;
  - (3) consolidating all of the client's bills into one reduced payment; and
  - (4) paying the client bills in a timely manner;
- ▲ counseling to every client as to budgeting their income and paying their bills in a timely manner;
- ▲ a monthly newsletter, which provides information on bi-weekly mortgage plan; tax tips; information pertaining to the credit bureaus, loan scams, repairing and
- ▲ restoring credit; budgeting; savings on prescription drugs, mortgages, groceries, etc.; and continued guidance and counseling.

Upon enrollment in its debt consolidation plan, clients receive a video that discusses topics such as bankruptcy laws, loan scams, rebuilding credit and debt consolidation.

XXX plans to offer its services to major corporations nationwide.

In addition, XXX plans to continue to donate money to the homeless and drug and alcohol abuse. Moreover, XXX contends that approximately 25 to 30 percent of its staff is composed of individuals who have "gone through an alcohol and drug abuse rehabilitation program."

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	Schedule or Exhibit No.
<b>Name of Taxpayer:</b> XXXXX		<b>Tax Year(s) Ended:</b> December 31, XXXX

**b. Sources of Financial Support**

With respect to its sources of financial support, XXX states that it does not accept donations from the general public. In lieu of public support, XXX states that it will rely on its clients' creditors for revenues in the form of "fair share" income, where creditors agree to pay XXX a monthly collection fee ranging between 10 and 15 percent of the amount XXX collects from its client on behalf of the creditors.

XXX also stated that creditors, by using a tax exempt credit counseling agency, as opposed to a collection agency, will save between 20 and 25 percent in collection fees.

In addition, XXX expects to derive revenues from enrolling consumers in its debt consolidation plan. The enrollment fee is \$ per client. The client also is assessed a monthly fee of \$ per month to cover expenses of postage, checks, wages, advertising, phones and general marketing expenses.

**c. Related Party Transactions**

During the exemption application process, XXX disclosed that it engaged in the following related party transactions:

- (1) Promissory Note for \$: dated January 1, XXXX, to purchase office equipment from XXXXX, Vice President of XXXXX and a family member of Director XXX.
- (2) Promissory Note for \$: dated January 1, XXXX, to purchase office and computer equipment from XXX.
- (3) Agreement with XXXXX, dated October 9, XXXX, to provide the following services:
  - Hiring and training sales agents;
  - Continuing training of sales agents;
  - Providing computer, phone and office equipment, office space and supplies necessary to market Debt Consolidation/credit Service;
  - Scheduling and handling all advertising, including newspaper, TV, radio and direct mail advertising;
  - Processing of clients acquired by XXXXX on behalf of XXX;
  - Marketing Debt Consolidation videos under XXX's name;

XXX did not obtain or provide the Service with an independent review for any of the disclosed related party transactions.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	Schedule or Exhibit No.
Name of Taxpayer:  XXXXX		Tax Year(s) Ended:  December 31, XXXX

**d. Service Response to XXX's Submission**

In a letter dated June 2, XXXX, the Service ruled that XXX was not organized and operated in furtherance of charitable, scientific, or educational purposes within the meaning of §501(c)(3).

In support of its decision, the Service cited the following reasons:

- ❖ XXX does not meet the organizational test of §501(c)(3) because XXX's purpose is too broad.
- ❖ XXX is not organized and operated for a charitable purpose. Rather, XXX is operated as a trade or business ordinarily carried on for profit. Moreover, XXX's services are provided to the general public without regard to financial status.
- ❖ XXX has failed to demonstrate that no part of its net earnings will inure to the benefit of private individuals.

**e. XXX's Resubmission of its Exemption Application**

In a letter dated July 26, XXXX, XXX's Power of Attorney, XXXXX stated that in any year in which XXX's revenues exceeds its expenses, the balance will be donated to one or more organizations described in §501(c)(3) as selected by XXX's board of directors.

In a letter dated August 18, XXXX, XXX's Power of Attorney, XXXXX stated that XXX did not have any related corporations, because the related party contract with XXXXX had been cancelled. Instead, XXX would perform the services on its own.

In a fax dated November 29, XXXX, XXX's Power of Attorney, XXXXX sent the Service a copy of XXX's Restated Articles of Incorporation, which corrected XXX's failure of the organizational test and restated XXX's purpose to be as follows:

- (1) To help reduce personal bankruptcy by informing the public on personal money management and consumer credit counseling;
- (2) To aid low income or unemployed individuals and families with fiscal problems;
- (3) To assist low income or unemployed individuals with debt consolidation and participate in corporate fair share programs;
- (4) To collect and otherwise raise money for the purposes stated herein;
- (5) To cooperate with federal, state and local government agencies to achieve the purposes stated herein; and
- (6) To do everything lawful, necessary, suitable and proper to attain the charitable purposes set forth herein.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer:</b> XXXXX		<b>Tax Year(s) Ended:</b> December 31, XXXX

**f. Recognition of Exemption Status**

Based upon XXX's statements and their actions taken to conform to the statutory requirements, the Service reconsidered its decision and in a letter dated December 2, XXXX, granted recognition of tax exempt status under §501(c)(3) with an advance ruling for foundation status of §509(a)(2).

At the conclusion of the advance ruling period, the Service confirmed XXX's foundation status as an organization described in §509(a)(2) with a letter dated January 7, XXXX.

**3. SUBSEQUENT CHANGES TO THE ARTICLES OF INCORPORATION**

On April 7, XXXX, the corporation's name was changed from "XXXXX." to "XXXXX"

On April 28, XXXX, XXX amended its articles of incorporation to add the office of Vice-President under Article Seven and named XXXXX as its registered agent under Article Twelve.

**4. OFFICERS AND DIRECTORS DURING THE YEAR OF EXAMINATION**

XXX states that since April XXXX, its board of directors has been changed to be entirely comprised of members from its community and that other than being a board member they do not have any ownership, affiliation or relationships with one another. XXX further provides that its board members do not participate in any of its day-to-day activities, but does meet once a year to discuss issues, give advice and oversight on policies and procedures.

The names, titles, addresses along with short biographical statement provided XXX about its officers and directors in XXXX are as follows:

Name	Title	Address
XXXXX	President/Chairman	XXXXX
A statement was not provided.		
XXXXX	Treasurer/Director	XXXXX
As XXX's Chief Operating Officer, Mr. XXXX is responsible for overseeing the operation of XXX. Mr. XXXX also is chairman of the Compensation/Transactions Committee. He is also employed by both XXXXX and XXXXX. His mother, XXXXX, is Vice -President of XXXXX.		

Form 886-A (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	Schedule or Exhibit No.
Name of Taxpayer: XXXXX		Tax Year(s) Ended: December 31, XXXX

Name	Title	Address
XXXXX	Secretary/Director	XXXXX
Mr. XXXXX graduated from XXXXX State University in XXXX, receiving a Bachelor of Science Degree in Criminal Justice. He began his career as a Loss Prevention Specialist, overseeing security technology and credit card fraud investigations. He began working at XXX in XXXX, overseeing banking functions and all other operational functions. On April 1, XXXX, the board of directors voted to make him the President of XXX.		
XXXXX	Director	XXXXX
A graduate of XXXXX in XXXXX in XXXX majoring in Business Management. Ms. XXXXX began her career with XXX. She led XXX in the development of processing management systems. Ms. XXXXX was instrumental in obtaining ISO approval-with no non-conformities. She left XXX to raise her family, but continues to serve and provide her insight to the operational issues facing XXX.		
XXXXX	Director	XXXXX
A senior level executive with over thirty years of experience in technology and related electronics manufacturing. Mr. XXXXX consulting clients include XXXXX, XXXXX, XXXXX and XXXXX. He was a member of the Board of Governors and a Group Vice President of the XXXXX. He has also served as Chairman of XXXXX, which led the revolution in miniaturization of two-way RF communications.		
XXXXX	Director	XXXXX
President of XXXXX whose clients include XXXXX, XXXXX, XXXXX, XXXXX, XXXXX and XXXXX. Mr. XXXXX started his career as an architectural designer with XXXXX in XXXX. He also was employed as senior designer/project manager at XXXXX.		
XXXXX	Director	XXXXX
The sole owner of XXXXX, an accounting firm that maintains the financial books and records of XXX, XXXXX and XXXXX. His firm also compiles the financial statements and prepares federal information and tax returns of all three entities.		
XXXXX	Director	XXXXX
Vice president of Retail Development at XXXXX, which is involved with commercial property development, management, acquisition and disposition. Mr. XXXXX holds a degree in Engineering and a degree in Finance from XXXXX University. He currently resides on the West Coast of XXXXX and commutes to various development sites in XXXXX.		

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	Schedule or Exhibit No.
Name of Taxpayer: XXXXX		Tax Year(s) Ended: December 31, XXXX

Name	Title	Address
XXXXX	Director	XXXXX
A graduate of XXXXX State University with a degree in Marketing in XXXX. He has served as an adjuster, fraud investigator and now operates his own XXXXXX Agency.		
XXXXX	Director	XXXXX
XXXXX provides technology consulting to improve business communication tools. Mr. XXXXX graduated from the University of XXXXX in XXXX. He has been instrumental in guiding XXX in its communications decisions.		
XXXXX	Director	XXXXX
A statement was not provided		
XXXXX	Director	XXXXX
A statement was not provided		

**5. COMPENSATION to OFFICERS AND DIRECTORS**

During the year ended December 31, XXXX, XXX's officers were paid as follows:

Officer Name	Title	Salary	Bonus	401K	Medical	Car Allowance
XXXXX	President	\$		\$		\$
XXXXX	Treasurer	\$		\$	\$	\$
XXXXX	Secretary	\$	\$	\$	\$	\$

XXX stated that the compensation paid to its officers is approved by both the compensation committee and the board of directors. Its decisions are based on the fair market value of compensation paid to officers in companies of similar size, both for-profit and non-profit. In addition, both bodies review and consider the report issued by R.D. Brown and Company, titled "Consumer Credit Counseling Industry, 1999 Compensation Survey." No further information was provided to support these statements. The remaining members of the board listed as Directors are not compensated.

XXX explained that the bonus compensation paid to Mr. XXXXX was based on overall company performance.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	Schedule or Exhibit No.
Name of Taxpayer: XXXXX		Tax Year(s) Ended: December 31, XXXX

**6. FORM 990**

The Service's records show that XXX has filed a Form 990 annually as required by law. The results from its operations during the five (5) year period between XXXX and XXXX are set forth below in Table A.

**Table A**  
**Form 990 - Income Statement**

	XXXX	XXXX	XXXX	XXXX	XXXX
Total Revenue	\$	\$	\$	\$	\$
Total Expenses	\$	\$	\$	\$	\$
Excess Earnings for the year	\$	\$	\$	\$	\$
Nets assets at beginning of year	\$	\$	\$	\$	\$
Nets assets at end of year	\$	\$	\$	\$	\$
Percentage increase in Net Assets From prior year.	% <sup>1</sup>				

<sup>1</sup> Percentage amounts were computed by the examining agent.

As detailed below in Table B, XXX received substantially all of its revenue during the five (5) year period from two sources: "fair share" payments from creditors and service fees charged to consumers enrolled in the debt management program.

**Table B**  
**Form 990 - Itemized Revenue Sources**

Revenues Per Form 990	XXXX	XXXX	XXXX	XXXX	XXXX
Contributions	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
DMP Fees & Fair Share	\$	\$	\$	\$	\$
Interest on Investments	\$ 0	\$ 0	\$	\$	\$
Net Sales of Inventory	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
<b>Total Revenue</b>	\$	\$	\$	\$	\$
Percentage change in Revenue from the prior year		% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>
Percentage change in DMP Fees & Fair Share from the prior year		% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>
Percentage of DMP Fees & Fair Share To Total Revenue		% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>

<sup>1</sup> Percentage amounts were computed by the examining agent.

Form <b>886-A</b> (Rev. January 1994)	<b>EXPLANATION OF ITEMS</b>	Schedule or Exhibit No.
<b>Name of Taxpayer:</b> XXXXX		<b>Tax Year(s) Ended:</b> December 31, XXXX

"Fair share" payments are generally described as revenues derived from the provision of debt consolidation services, the cost of which is supported by payments from the credit industry. These payments are generally paid by the credit industry and are usually calculated as a percentage of the approved monthly payment remitted through the plan. Also, the rates used for calculating payments are set individually by each creditor. Therefore, they can vary widely from one creditor to the next. Additionally, while the majority of financial and department stores, who offer credit services to customers, participate in making "fair share" payments; many smaller businesses such as doctors, dentists, lawyers and hospitals, do not.

In contrast, debt management fees are revenues derived from consumers participating in the debt consolidation service. The fees include an initial enrollment charge and a monthly fee, fixed in amount, that is payable to the credit counseling agency at the time the consumer makes his or her consolidated debt payment.

The financial records provided to the Service do not distinguish revenue derived from different activities or sources for the year under examination.

Table C below sets forth a summary of XXX's expenses reported for the five year period ending December 31, XXXX.

**Table C**  
**Form 990 - Total Expenses**

Expenses Per Form 990	XXXX	XXXX	XXXX	XXXX	XXXX
Program Service	\$	\$	\$	\$ 15,139,413	\$17,077,856
Management and General	\$	\$	\$	\$ 306,537	\$ 369,195
<b>Total Expenses</b>	\$	\$	\$	\$15,445,950	\$17,447,051
Percentage change in Expenses from the Prior Year		% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>
Percentage change in Program Service from the prior year		% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>
Percentage of Program Service to total expenses	% <sup>-1</sup>	% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>	% <sup>1</sup>

<sup>1</sup>. Percentage amounts were computed by the examining agent

Table D below sets forth a summary of XXX's itemized expenses reported for the five year period ending December 31, XXXX.

EXPLANATION OF ITEMS

Name of Taxpayer:

XXXXX

Tax Year(s) Ended:

December 31, XXXX

**Table D**  
**Form 990 - Itemized Expenses**

Description	XXXX	XXXX	XXXX	XXXX	XXXX
Grants and allocations	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Compensation of officers, directors	\$	\$	\$	\$	\$
Other salaries and wages	\$	\$	\$	\$	\$
Pension plan contributions	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Other employee benefits	\$	\$	\$	\$	\$
Payroll taxes	\$	\$	\$	\$	\$
Professional fundraising fees	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Accounting fees	\$	\$	\$	\$	\$
Legal fees	\$	\$	\$	\$	\$
Supplies	\$	\$	\$	\$	\$
Telephone	\$	\$	\$	\$	\$
Postage and shipping	\$	\$	\$	\$	\$
Occupancy	\$	\$	\$	\$	\$
Equipment rental and maintenance	\$	\$	\$	\$	\$
Printing and publications	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Travel	\$	\$ 0	\$ 0	\$ 0	\$ 0
Conferences, conventions & meetings	\$	\$ 0	\$ 0	\$	\$
Interest	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Depreciation, depletion, etc.	\$	\$	\$	\$	\$
Other-					
Advertising	\$	\$	\$ 0	\$ 0	\$ 0
Auto expense	\$	\$	\$	\$	\$
Bank service charges	\$	\$	\$	\$	\$
Communication services	\$ 0	\$	\$	\$	\$
Consulting expenses	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Customer service/processing	\$ 0	\$	\$	\$	\$
Donations	\$ 0	\$	\$	\$	\$
Dues & subscriptions	\$ 0	\$	\$	\$	\$
Insurance	\$ 0	\$	\$	\$	\$
License & fees	\$ 0	\$	\$	\$	\$
Office expense	\$ 0	\$	\$	\$	\$
Public awareness/education	\$ 0	\$	\$	\$	\$
Taxes - other	\$ 0	\$ 0	\$ 0	\$ 0	\$
Utilities	\$ 0	\$	\$	\$	\$
Other	\$				
<b>Total Expenses</b>	\$	\$	\$	\$	\$

<sup>1</sup> Percentage amounts were computed by the examining agent.

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Table E sets forth XXX's total of functional expenses reported on its Form 990 for the year ended December 31, XXXX and the portion it allocated to "Program Services" as the cost of accomplishing its exempt purposes.

**Table E**  
**Statement of Functional Expenses reported on Form 990 TYE XXXX**

Line Item Description	Program Service Expenditures			
	(A) TOTAL Expense Item	% of Total Expenses <sup>1</sup>	(B) Allocated to Program Services	% to Line Item Expense <sup>1</sup>
Grants and allocations				
Compensation of officers, directors, etc	\$	%	\$ 0	-
Other salaries and wages	\$	%	\$	%
Pension plan contributions	\$ 0		\$ 0	
Other employee benefits	\$	%	\$	%
Payroll taxes	\$	%	\$	%
Professional fundraising fees	\$ 0		\$ 0	
Accounting fees	\$	%	\$	%
Legal fees	\$	%	\$	%
Supplies	\$	%	\$	%
Telephone	\$	%	\$	%
Postage and shipping	\$	%	\$	%
Occupancy	\$	%	\$	%
Equipment rental and maintenance	\$	%	\$	%
Printing and publications	\$ 0		\$ 0	
Travel	\$ 0		\$ 0	
Conferences, conventions, & meetings	\$	%	\$	100.00 %
Interest			\$ 0	-
Depreciation, depletion, etc.	\$	%	\$ 0	-
<b>Subtotal before Other expenses</b>	<b>\$</b>	<b>%</b>	<b>\$</b>	<b>-</b>
Other expenses:	\$ 0		\$ 0	-
Auto expense	\$	%	\$	%
Bank service charges	\$	%	\$	%
Communication services	\$	%	\$	%
Customer service/processing	\$	%	\$	%
Donations	\$	%	\$	%
Dues & subscriptions	\$	%	\$	%
Insurance	\$	%	\$	%
License & fees	\$	%	\$	%
Office expense	\$	%	\$	%
Public awareness/education	\$	%	\$	%
Utilities	\$	%	\$	%
<b>Subtotal other expenses</b>	<b>\$</b>	<b>%</b>	<b>\$</b>	<b>%</b>
<b>Total Expenses</b>	<b>\$</b>	<b>100.00 %</b>	<b>\$</b>	<b>%</b>

<sup>1</sup> Percentage amounts were computed by the examining agent.

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Payments to XXXXX and XXXXX, the related entities owned by XXX, are distributed among several categories such as customer service/ processing services, communication services and public awareness/ education expenses.

Customer service and processing encompass DMP management activities, while Public awareness/ education expense represents XXX's advertising/ promotional activities. All advertising placements are arranged by XXXXX.

## **7. ACTIVITIES**

### **a. Operations**

XXX states that it is operated to provide debt consolidation and credit counseling services to individuals and families who are financially distressed.

During the year under examination, XXX operated as a call center staffed with employees it classifies as "credit counselors." The call center primarily received inbound phone calls originated by consumers in response to a marketing offer presented via print, radio, television or other media such as the internet. Employees also were required to make outbound phone calls to individuals (1) whose names were referred to the call center by a third party such as a creditor or (2) who requested to be contacted during a previous call, by e-mail or through the internet .

For the XXXX tax year, XXX provides that its counselors handled approximately 4,000 calls per week, with less than 10 percent of those calls resulting in the enrollment of an individual onto a DMP. Conversely, almost 90 percent of XXX's counseling calls did not result in a DMP. Regardless of the outcome, XXX claims that it counseled all callers.

XXX provided a computerized record of telephone calls, all of which did not result in a DMP enrollment. An analysis of this data was conducted and a summary of these results were previously provided to XXX, identifying the following statistics:

**Table 1**  
**Summary of Telephone records**

Total Number of Identified Callers.	
Average Duration for each Call.	Min
Average Number of Calls per Identified Caller.	
Total of Average Call duration per each Identified Caller.	Min

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**Telephone records stratified by Duration**

Total of Calls of Less than or equal to 5 Minutes.	%
Total of Calls of 15 Minutes or Less but greater than 5 Minutes.	%
Total of Calls of 30 Minutes or less but greater than 15 Minutes.	%
Total of Calls of 60 Minutes or less but greater than 30 Minutes.	%
Total of Calls of greater than 60 minutes.	%

**b. Services**

XXX was unable to provide a copy of its web site as it appeared during XXXX. Over the past 18 months, the web site has been frequently updated to add or edit its content. XXX does not have a policy to maintain records or back-up copies of web page modifications that would show its past content or presentation.

The web site currently describes their services as:

**Personal Budgeting:** Sometimes you can resolve a debt problem by managing your money more effectively. Personal Budgeting could be the answer to your debt problems. Learn ways to identify overspending and how to create a personal budget."

**Debt Management Program:** A consumer credit counseling service helping individuals consolidate unsecured debt into one easy payment so that they can get out of debt in 4 to 5 years. In addition to lowering monthly payments, many creditors will reduce or eliminate interest and stop charging late fees. Most importantly, past due accounts will be re-aged, that is, shown as current."

**Home Equity Loan** may be recommended for home owners with equity and a large amount of unsecured debt. Our certified credit counselors can advise you on how to best proceed with getting your home equity loan."

**Credit Card Promos:** can help you obtain lower interest rates and save money on credit card payments. Our consumer credit counseling service can list the advantages and disadvantages of this method of credit management."

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"Debt Settlement: can be a way to get out of debt quickly; however, this debt solution can have a negative effect on your credit. Our certified credit counselors will review your financial situation to determine if debt settlement is the right option and refer you to a reputable debt settlement firm in good standing with the Better Business Bureau."

"Bankruptcy: should only be attempted after exhausting all other debt solutions, because bankruptcy will remain on your credit history for ten years. Our credit counseling service will examine all your credit options to help you decide if filing bankruptcy is the correct decision for you."

Each topic, in turn, links to a page that provides a brief explanation and generally contains a statement that another alternative may be a debt management plan and a link to the "contact us" page.

*" ...Our debt management program helps consumers get back on track with their bills by consolidating their unsecured debt into one easy monthly payment. Our credit counseling agency advises consumers on personal budgeting, debt consolidation through home equity loans, debt settlement, credit card promos and filing bankruptcy. Any one of these credit solutions can help consumers get through financial difficulties."*

*Our non-profit credit counseling agency provides additional educational resources and materials on credit management, debt collection and money management. Credit and money management is key to creating a stable, financial future. For consumers in debt collection, it is important for them to know their consumer rights and how to spot collection harassment so debt collectors don't take advantage. Our credit counseling agency encourages consumers to enhance their personal financial literacy through our educational resources."*

XXX explained that when a person calls seeking assistance, an employee will review their unsecured debt, such as Major Credit Cards, Department Store Cards, Medical Bills, or Loans that have no collateral or co-signers, personal income as well as household expenses and determine if they would be suited for a debt management program.

This task is facilitated through the use of a software program called the 'Interactive Counseling Tool' (Tool). The Tool software was developed by and is owned by XXXXX, which leased it to XXX as part of their service agreement.

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The Tool, as presented, guides an employee to complete following tasks:

- Informs the client about our organization;
- Collects contact information;
- Completes a budget analysis;
- Completes a debt to income analysis;
- Qualifies the consumer for the appropriate solution;
- Describes the details of the solution;
- Gives instructions and any information that is required;
- Sets follow up appointment, if needed;
- Sends (DMP) agreement, if required; and
- Starts referral process, if required.

The page shown below is from their current tool's "Application Process" screen.

**Interactive Counseling Tool**

The tool program can collect a significant amount of information about a caller, yet very little of it is necessary for an employee to establish a debt management plan for any caller. There is no indication that callers are screened in a way to limit participation to those individuals who are considered "low income" or any other criteria,

The Tool permits the counselor to choose among six different reasons for joining the program and includes a section where counselors can input what XXX calls "Special Hardship Notes."

After XXX's employee collects the "Income," "Assets" and up to six "Expense" items from a caller, the Tool uses the data to produce a debt to income analysis, which can be used as a basis for recommending a solution.

Table 2 below shows a description and number of callers who were provided the services and solutions XXX states that it completed during XXXX. The only figure reported on this list that was confirmed by other records is the debt management program solution.

**TABLE 2**

Solutions offered during XXXX	Callers
Debt Management Program	1 %
Financial Counseling	%

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Financial Budgeting	%
Bankruptcy Assistance Referral	%
Mortgage Assistance Referral	%
Auto Payment Assistance Referral	%
Student Loan Referral	%
Government Income Assistance Referral	%
Loan Referral	%
IRS Referral	%
No Assistance	%
<b>Total Calls</b>	<b>%</b>

If a call cannot be completed it is saved for future action by placing the account file record into categories such as "Prospect," "Creditors," or "Call Back Info".

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**(1) The DMP Solution**

To qualify for its debt management program during XXXX, XXX required callers to have a minimum of at least \$2,000 of unsecured debt. While not included in this list, the caller must also have sufficient income to pay the proposed new monthly payment. In addition, the caller must also satisfy any restrictions imposed by each of their creditors.

After the counselor determines that the caller is qualified for the debt management program, an information packet for DMP enrollment is mailed or sent by fax to the caller for review. The information packet relates entirely to facilitating the establishment of the debt management plan.

XXX's employee will also advise the potential client that only upon receipt of their completed documents and payment of the set-up/ enrollment fee, will each of their creditors be contacted to advise them of the client's enrollment in the plan and to make a payment proposal. Once the plan has been approved by each of their creditors, funds will then be promptly disbursed. In addition, participants will begin to receive a monthly statement detailing their transaction activity.

Although the print is quite small, the "Debt Management Agreement" does directly state the amount of the DMP Enrollment fee, the new monthly debt payment and that the monthly service fee is included in the new monthly debt payment

XXX provided the Service the following information about the debt management program, as set forth below in Table 3.

**Table 3**  
**DMP Client Statistics**

**Active DMP Clients, 1-01-XXXX**

**Add:**

New Clients in CY XXXX

Reinstated Clients in CY XXXX

Total Additions

**Less:**

Client Cancelled on Verification

Bankrupt

Voluntarily Cancelled by Client

Dropped by Creditor/XXX

Paid in Full

Total Subtractions

**Active DMP Clients, 12-31-XXXX**

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Table 4 below sets forth statistics regarding the success rate of XXX's DMP program:

**Table 4  
DMP Success Rate**

Description	XXXX DMP Clients	Total DMP Clients
a) Cancel within 6 Months	-- %	
b) Cancel between 7-12 Months	%	
c) Cancel between 13-24 Months	%	
e) Completed on the Program - Paid in Full	%	%
f) Completed off the Program - Voluntary Cancel	%	%

**(2) Other XXX Solutions**

Additional analysis of the computerized telephone records that did not result in a DMP enrollment shows other outcomes XXX utilized for consumer calls during XXXX. In this report records were removed because they were identified as having been accessed related to a review of the record's processing history or status.

The remaining data of call comments can be grouped as follows:

DESCRIPTION	Average Call Duration <small>HH:MM:SS)</small>	Aggregate Average Duration of All Calls <small>HH:MM:SS)</small>	Total Call Count	% of Total Calls
Comment indicates a DMP Qualified Caller:				
Application Re-sent	0:03:49	0:45:51	5,490	1.67 %
Application Sent	0:30:22	6:04:21	5,105	1.55 %
Client Can Handle	0:04:40	0:56:01	4,861	1.48 %
Client Turned Down Services	0:06:03	1:12:41	4,586	1.39 %
Not Interested - Financial Counseling Only	0:03:57	0:47:23	32,222	9.80 %
Subtotal	0:09:46	9:46:17	52,264	15.89 %

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The comment data also provides the following additional information about XXX's debt management plan's enrollment rate.

DESCRIPTION  Comment indicates Caller is Not Qualified for the DMP program.	Average Call Duration <small>HH:MM:SS</small>	Aggregate Average Duration of All Calls <small>HH:MM:SS</small>	Total Call Count	% of Total Calls
Not Qualified	0:08:18	1:39:33	7,444	2.26 %
Not Qualified - Financial Counseling Only	0:03:57	0:03:57	1	0.00 %
Referred for Other Action	0:05:14	1:02:45	820	0.25 %
Referred to Website	0:07:32	1:30:25	194	0.06 %
Subtotal	0:06:15	4:16:39	8,459	2.57 %

Undetermined Qualification for the DMP program.	Average Call Duration <small>HH:MM:SS</small>	Aggregate Average Duration of All Calls <small>HH:MM:SS</small>	Total Call Count	% of Total Calls
Budget/Credit Counseling	0:00:00	0:00:00	1	0.00 %
Call Back	0:04:47	0:57:26	232,623	70.72 %
Can Not Reach	0:02:16	0:27:13	10,688	3.25 %
Client Will Call Back	0:06:20	1:16:01	3,843	1.17 %
Financial & Budget Counseling	0:02:55	0:35:02	15,443	4.70 %
Followed Up	0:01:25	0:01:25	2	0.00 %
Hung Up	0:05:19	1:03:50	2,469	0.75 %
No calls/No Emails	0:03:40	0:43:57	2,975	0.90 %
Non Working Phone Number	0:01:36	0:03:13	85	0.03 %
Not A US Residence	0:02:16	0:04:32	13	0.00 %
Not At This Phone Number	0:01:49	0:03:37	49	0.01 %
SubTotal	0:02:57	5:16:17	268,191	81.54 %

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All Comments	Average Call Duration <small>HH:MM:SS</small>	Aggregate Average Duration of All Calls <small>HH:MM:SS</small>	Total Call Count	% of Total Calls
<b>Totals</b>	0:04:39	19:19:13	328,914	100%

**8. ADVERTISING**

XXX's advertising includes the placement of Ads in the phone directories of major markets, Radio spots nationwide and TV commercials. Below is a sample of their content:

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XXX also places radio spots nationwide, a sample of which is provided below:

**XXX 60 second radio spot script**

**Exercising couple:** We were over our heads in credit card debt and looking for a way out. A number of companies said they would help us, but they were only interested in charging huge upfront fees and putting us further in debt. XXXXX was different.

**Voiceover:** XXXXX won't put you further into debt. As a nonprofit service we've helped thousands of people for over 11 years. We work with you and your creditors to reduce your monthly payments so you can get on with life.

**Woman:** XXXXX cut my monthly payments in half.

**Woman:** They cut my interest rates from an average of 23 percent to 8 percent, some even to zero. I'll be out of debt in four years instead of twenty. XXXXX saved me over \$13,000 in interest fees alone.

**Operator:** Call now to reduce your monthly payments, cut the interest rates on your credit cards by up to half and get your unsecured debt paid off years earlier.

**Voiceover:** Certified counselors are standing by. Don't you owe it to yourself to work with a real non-profit service? Call now to find out how to receive a free credit report. Call 800...

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**9. EDUCATIONAL MATERIALS/SEMINARS:**

The Service requested documentation of educational activities such as materials distributed, seminars conducted and any other outreach directed at the public especially with regard to making contact with those of "Low income" to aid with improving their management and use of credit.

XXX provided a list of its "Education, Community Outreach and Training Initiatives" that occurred during XXXX. Two (2) items state "Placed literature in program". One (1) states "advertised in magazine" of a Trade Association. One (1) states that the players and families in the counties' Parks & Recreation softball league were referred for free credit counseling help. This outreach is facilitated by XXX's sponsorship of a team in the league. The remaining items describe meetings with organizations or trade associations whose membership may have contact with clients who could have a need for credit counseling. The general purpose of these meetings is to establish a relationship with the organization to develop programs that will assist its members to supply this information to their clientele. XXX's program proposals included providing some training about credit counseling issues, raising awareness in the industry about these needs and that XXX can directly provide these services and encouraging its members to make referrals to XXX. Information regarding the success of these activities was not provided.

XXX also provided copies of the following nine (9) pamphlets:

TITLE	Number of Pages
Shopping & Saving	
Make the most of your credit score	
Happy Holidays! Strategies for a Less Stressful Less Expensive Holiday Season.	
Rebuilding Good Credit	
Divorce & Your Credit	
Credit Cards: What You Need to Know	
New Families & Finances	
Budgeting: Your Money Guide for Getting Through School	

Each pamphlet provides a brief overview of the topic and the key issues relative to the title.

No other information was submitted.

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**LAW:**

Section 501(c)(3) of the Code exempts from federal income tax, corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting to influence legislation, and which does not participate in, or intervene in any political campaign on behalf of any candidate for public office.

Section 6001 of the Code provides that every person liable for any tax imposed by this title, or for the collection thereof, shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. Whenever in the judgment of the Secretary it is necessary, he may require any person, by notice served upon such person or by regulations, to make such returns, render such statements, or keep such records, as the Secretary dXXXs sufficient to show whether or not such person is liable for tax under this title.

The term charitable includes relief of the poor and distressed. Income Tax Regs. Section 1.501(c)(3)-1(d)(2).

The term educational includes (a) instruction or training of the individual for the purpose of improving or developing his capabilities and (b) instruction of the public on subjects useful to the individual and beneficial to the community. Treas. Reg. § 1.501(c)(3)-1(d)(3). In other words, the two components of education are public education and individual training.

Section 1.501 (c)(3)-1 (a)(1) of the Regulations provides that, in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501 (c)(3)-1(c)(1) of the Regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. The existence of a substantial nonexempt purpose, regardless of the number or importance of exempt purposes, will cause failure of the operational test. Better Business Bureau of Washington. D.C. v. U.S., 326 U.S. 279 (1945).

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In Better Business Bureau of Washington D.C., Inc. v. United States, supra, The Court found that the organization had an "underlying commercial motive" that distinguished its educational program from that carried out by a university.

In American Institute for Economic Research v. United States, 302 F. 2d 934 (Ct. Cl. 1962), the Court considered the status of an organization that provided analyses of securities and industries and of the economic climate in general. The organization sold subscriptions to various periodicals and services providing advice for purchases of individual securities. Although the court noted that education is a broad concept, and assumed for the sake of argument that the organization had an educational purpose, it held that the organization had a significant nonexempt commercial purpose that was not incidental to the educational purpose and was not entitled to be regarded as exempt.

An organization must establish that it serves a public rather than a private interest and "that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests." Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii). Prohibited private interests include those of unrelated third parties as well as insiders. Christian Stewardship Assistance, Inc. v. Commissioner, 70 T.C. 1037 (1978); American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989). Private benefits include an "advantage; profit; fruit; privilege; gain; [or] interest." Retired Teachers Legal Fund v. Commissioner, 78 T.C. 280, 286 (1982).

An organization formed to educate people in Hawaii in the theory and practice of "est" was determined by the Tax Court to be part of a "franchise system which is operated for private benefit," and, therefore, should not be recognized as exempt under section 501(c)(3) of the Internal Revenue Code. est of Hawaii v. Commissioner, 71 T.C. 1067, 1080 (1979). Although the organization was not formally controlled by the same individuals who controlled the for-profit entity that owned the license to the "est" body of knowledge, publications, and methods, the for-profit entity exerted considerable control over the applicant's activities by setting pricing, the number and frequency of different kinds of seminars and training, and providing the trainers and management personnel who are responsible to it, in addition to setting the price for the training. The court stated that the fact that the organization's rights were dependent upon its tax-exempt status showed the likelihood that the for-profit entities were trading on that status. The question for the court was not whether the payments made to the for-profit were excessive, but whether the for-profit entity benefited substantially from the operation of the organization. The court determined that there was a substantial private benefit because the organization "was simply the instrument to subsidize the for-profit corporations and not vice versa and had no life independent of those corporations."

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Private benefit does not necessarily involve the flow of funds from an exempt organization to a private party. Rev. Rul. 76-206, 1976-1 C.B. 154, considered an organization formed to promote broadcasting of classical music in a particular community. The organization carried on a variety of activities designed to stimulate public interest in the classical music programs of a for-profit radio station, and thereby enable the station to continue broadcasting such music. The activities included soliciting sponsors, soliciting subscriptions to the station's program guide, and distributing pamphlets and bumper stickers encouraging people to listen to the station. The organization's board of directors represented the community at large and did not include any representatives of the for-profit radio station. The revenue ruling concludes that the organization's activities enable the radio station to increase its total revenues and therefore benefit the for-profit radio station in more than an incidental way. Therefore, the organization is serving a private rather than a public interest and does not qualify for exemption.

In International Postgraduate Medical Foundation v. Commissioner, the Tax Court held that the exempt status of a corporation under IRC 501(c)(3) was properly revoked because the corporation was not operated exclusively for exempt purposes. The corporation conducted continuing medical educational tours abroad. The purposes of the corporation consisted of 1) providing benefits to a for-profit travel agency that arranged tours for the corporation's seminars, and 2) providing sightseeing and recreational activities. The corporation was formed by the owner of the travel agency to obtain customers for his business. The owner controlled the corporation and exercised that control to benefit his travel agency.

The Service has issued two rulings holding credit counseling organizations to be tax exempt. Rev. Rul. 65-299, 1965-2 C.B. 165, granted exemption to a section 501(c)(4) organization whose purpose was to assist families and individuals with financial problems and to help reduce the incidence of personal bankruptcy. Its primary activity appears to have been meeting with people in financial difficulties to "analyze the specific problems involved and counsel on the payment of their debts." The organization also advised applicants on proration and payment of debts, negotiated with creditors and set up debt repayment plans. It did not restrict its services to the needy. It made no charge for the counseling services, indicating they were separate from the debt repayment arrangements. It made "a nominal charge" for monthly prorating services to cover postage and supplies. For financial support, it relied upon voluntary contributions from local businesses, lending agencies, and labor unions.

Rev. Rul. 69-441, 1969-2 C.B. 115, granted section 501(c)(3) status to an organization with two functions: it educated the public on personal money management, using films, speakers, and publications, and provided individual counseling to "low-income individuals and families. " As part of its counseling, it established budget plans, i.e., debt management plans, for some of its clients.

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The services were provided without charge. The organization was supported by contributions primarily from creditors. By virtue of aiding low income people, without charge, as well as providing education to the public, the organization qualified for section 501(c)(3) status.

In the case of Consumer Credit Counseling Service of Alabama, Inc. v. U.S., 44 A.F.T.R. 2<sup>nd</sup> 78-5052 (D.D.C. 1978), the District Court for the District of Columbia held that a credit counseling organization qualified as charitable and educational under section 501(c)(3). It fulfilled charitable purposes by educating the public on subjects useful to the individual and beneficial to the community. Treas. Reg. § 1.501(c)(3)-1(d)(3)(i)(b). For this, it charged no fee. The court found that the counseling programs were also educational and charitable; the debt management and creditor intercession activities were "an integral part" of the agencies' counseling function and thus were charitable and educational. Even if this were not the case the court viewed the debt management and creditor intercession activities as incidental to the agencies' principal functions, as only approximately 12 percent of the counselors' time was applied to debt management programs and the charge for the service was "nominal." The court also considered the facts that the agency was publicly supported and that it had a board dominated by members of the general public as factors indicating a charitable operation. See also, Credit Counseling Centers of Oklahoma, Inc. v. United States, 79-2 U.S.T.C. 9468 (D.D.C. 1979), in which the facts and legal analysis were virtually identical to those discussed above in Consumer Credit Counseling Centers of Alabama, Inc. v. United States.

The organizations included in the above decision waived the monthly fees when the payments would cause a financial hardship. The professional counselors employed by the organizations spent about 88 percent of their time in activities such as information dissemination and counseling assistance rather than those connected with the debt management programs. The primary sources of revenue for these organizations were provided by government and private foundation grants, contributions, and assistance from labor agencies and United Way.

Outside the context of credit counseling, individual counseling has, in a number of instances, been held to be a tax-exempt charitable activity. Rev. Rul. 78-99, 1978-1 C.B. 152 (free individual and group counseling of widows); Rev. Rul. 76-205, 1976-1 C.B. 154 (free counseling and English instruction for immigrants); Rev. Rul. 73-569, 1973-2 C.B. 179 (free counseling to pregnant women); Rev. Rul. 70-590, 1970-2 C.B. 116 (clinic to help users of mind-altering drugs); Rev. Rul. 70-640, 1970-2 C.B. 117 (free marriage counseling); Rev. Rul. 68-71, 1968-1 C.B. 249 (career planning education through free vocational counseling and publications sold at a nominal charge). Overwhelmingly, the counseling activities described in these rulings were provided free, and the organizations were supported by contributions from the public.

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In Rev. Rul. 72-369, 1972-2 CB 245 denied exemption to an organization that provided managerial and consulting services on a regular basis for a fee as a trade or business ordinarily carried on for profit. The fact that the services in this case are provided at cost and solely for exempt organizations is not sufficient to characterize this activity as charitable within the meaning of section 501(c)(3) of the Code. Furnishing the services at cost lacks the donative element necessary to establish this activity as charitable within the meaning of section 501(c)(3) of the Code.

The Credit Repair Organizations Act (CROA), 15 U.S.C. § 1679 *et seq.*, effective April 1, 1997, imposes restrictions on credit repair organizations, including forbidding the making of untrue or misleading statements and forbidding advance payment, before services are fully performed. 15 U.S.C. § 1679b. Significantly, section 501(c)(3) organizations are excluded from regulation under the CROA.

The CROA defines a credit repair organization as:

- (A) any person who uses any instrumentality of interstate commerce or the mails to sell, provide, or perform (or represent that such person can or will sell, provide, or perform) any service, in return for the payment of money or other valuable consideration, for the express or implied purpose of -
  - (i) improving any consumer's credit record, credit history, or credit rating, or
  - (ii) providing advice or assistance to any consumer with regard to any activity or service described in clause (i).

15 U.S.C. § 1679a(3). The courts have interpreted this definition broadly to apply to credit counseling agencies. The Federal Trade Commission's policy is that if an entity communicates with consumers in any way about the consumers' credit situation, it is providing a service covered by the CROA. In Re National Credit Management Group, LLC, 21 F. Supp. 2d 424, 458 (N.D.N.J. 1998).

Businesses are prohibited from cold-calling consumers who have put their phone numbers on the National Do-Not-Call Registry, which is maintained by the Federal Trade Commission. 16 C.F.R. §310.4(b)(1)(iii)(B); 47 C.F.R. §64.1200(c)(2). Organizations having exemption under IRC Section 501(c)(3) are not subject to either of these restrictions.

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**DISCUSSION and ANALYSIS:**

In order for an organization to be described in §501(c)(3), it must be organized and operated substantially for applicable purposes thereunder. The presence of a single non-exempt purpose, if substantial, prohibits exemption. The burden of demonstrating continued entitlement to recognition under §501(c)(3) lies with the organization.

In XXXX, XXX applied for recognition of tax-exempt status under §501(c)(3) and was initially denied such recognition. In a letter dated June 2, XXXX, the Service ruled that XXX was not organized and operated in furtherance of charitable, scientific, or educational purposes within the meaning of §501(c)(3) for the following reasons:

- XXX does not meet the organizational test of §501(c)(3) because XXX's purpose is too broad.
- XXX is not organized and operated for a charitable purpose. Rather, XXX is operated as a trade or business ordinarily carried on for profit. Moreover, XXX's services are provided to the general public without regard to financial status.
- XXX has failed to demonstrate that no part of its net earnings will inure to the benefit of private individuals, viz., the agreement between XXX and XXXXX when XXX is an officer of both entities.

The Service recognized XXX as exempt under §501(c)(3) only after XXX addressed and resolved the Service's concerns as follows:

- XXX amended its articles of incorporation to conform to the organizational requirements of §501(c)(3);
- XXX agreed to donate its excess funds balance in any year in which its revenues exceeds its expenses to one or more organizations described in §501(c)(3) as selected by XXX's board of directors; and
- XXX cancelled the related party transaction between it and XXXXX and stated that it would perform the services itself.

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**Exempt Purpose**

The purpose of XXX's activities differs substantially from those of the organizations in Rev. Rul. 65-299, Rev. Rul. 69-441, and Consumer Credit Counseling Service of Alabama, Inc. v. U.S. In this case, XXX has engaged in minimal, if any, activities which further an exempt purpose. For example, its "counseling" activity is nothing more than a sales activity that screens consumers to determine whether they qualify to participate in the debt management program.

Another factor supporting the Service position is role of XXX's call center employees. These employees are essentially data entry clerks instructed in facilitating their use of their computerized software program to collect and input a callers' personal and financial information into the "Interactive Application Tool" to determine whether such callers will qualify for a DMP and to quickly determine the savings the potential client could expect. This "Budget Analysis" is merely a sales technique for obtaining the information from the consumer necessary for a determination to be made.

This is supported by several indicators that exist in XXX's own records.

First, an analysis of their telephone records of calls that did not result in DMP enrollment.

Overall, the average call duration of these records was about 4 ½ minutes in duration. The average number of calls each person made to speak with an employee was four (4) times. Thus, the aggregate amount of time that an average person spent with a call center employee providing their financial information is approximately 18 minutes. Based upon the complex and personal nature of an individual's finances it is incomprehensible that any substantive counseling can occur during such a time frame. Next, this same call records contained nearly eight thousand entries labeled as "Not Qualified". The average time of these calls was even shorter at 8 ½ minutes. Also, this call information showed that only 6 percent of the phone calls were greater than 15 minutes.

XXX qualifies th that the amount of time reflected on the computer records is not a precise measurement of the time for the length of a contact because it does not include the calls that did result in the caller's enrollment into the debt management program. The amount of time reflected in these records will almost always be less than the actual time spent, as usually telephone calls will have already commenced before a computer file is created for the caller by the employee.

This same fact has been used by several organizations in the credit counseling industry to promote that it only takes 20 minutes to lower your monthly payment, lower the interest rates on your outstanding credit balances, etc.

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Inspection of XXX's personnel records indicated that job applicants with prior counseling training and experience or knowledge of the finance industry are not targeted by XXX but rather hires applicants who, at a minimum, have a high school diploma and some form of customer service or sales experience.

In addition, XXX's 2 week training program for new "counselors" is composed primarily of introducing them to telemarketing sales techniques, improving their interpersonal communication skills and in the use of the Interactive Counseling Tool software program.

Thus, XXX did not provide any type of training about counseling methods, financial management or even case management, despite the claim that XXX counsels, on average, 1,000 callers per day.

Finally, call center employees were paid on a commission basis, i.e., paid for enrolling callers into the debt management program. Even XXX's minutes of meeting of the board of directors refers to its call center as the "Sales Counselor department." Generally, commission-based employees would be more concerned with making a sale than in providing education free of charge.

Another factor indicating a nonexempt purpose is the fact that XXX doesn't limit its marketing and selling of DMPs to low income people. Any consumer who can afford the payments is eligible for XXX's debt management program. There is no process to either screen callers by income level or a process to provide any waiver of fees for persons who were unable to afford its services.

XXX's obtained its exemption with the claim that it would be primarily educating the public on such topics as budgeting, strategies to improve their monetary skills and providing debt management services to assist those individuals in need of more in-depth instruction to resolve their financial problems. However, XXX did not demonstrate that it engaged in any meaningful educational outreach directed to the general public during XXXX. The list of events submitted as outreach and education can be summarily described as the marketing of their product, the debt management plan, to broaden the network to find where potential customers can be found.

XXX distributed a minor fraction of its excess fund balance in any year reviewed as it stated it would in its amended application. For instance, in XXXX XXX distributed only \$5,482 in grants but reported an excess fund balance for the year of \$654,602.

By inspecting client account file records and monitoring phone calls showed that the primary focus of employees was on analyzing whether or not the consumer would qualify for a DMP.

Substantially all of XXX's revenues are derived from fair share payments from creditors and fees charged to debt management clients. XXX does not solicit

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contributions from the general public, grants from governmental agencies or private foundations.

XXX contends that its software program is an integral part of the process of determining the appropriate solution for each caller. However, how this result was achieved in the time spent on a phone call.

**Substantial Non-Exempt Purpose**

XXX had a substantial non-exempt purpose of selling a product, the DMP, and of providing substantial business to XXXXX, the back end processing company owned by XXX. XXX was not furthering any charitable or educational purpose by mass marketing a DMP. XXX advertises in order to increase its business. Employees were not instructed on how to provide educational counseling during their training. Because the DMP and necessary concomitant collection activity constitute the overwhelming activities being carried on by XXX, it has operated and continues to operate for substantial non-exempt purposes. See Better Business Bureau of Washington D.C. Inc. v. United States and American Institute for Economic Research v. United States.

The reason XXX is organized as an exempt organization under §501(c)(3) of the Internal Revenue Code is to avoid the regulatory scheme of the Credit Repair Organizations Act (CROA), 15 U.S.C. section 1679, et. Seq. CROA was enacted to protect consumers by banning certain deceptive practices in the credit counseling industry. Had XXX been organized as a for-profit company, the CROA would prohibit it from charging fees in advance of fully providing services. Because §501(c)(3) organizations are exempted from the provisions of CROA, XXX is able to engage in the same deceptive business practices that Congress intended to prohibit when it passed the CROA law. As such, XXX is operated for a substantial non-exempt purpose: that of carrying on a business while avoiding federal regulations. In addition, XXX could not collect "fair share" payments from creditors if it did not have tax-exempt status. The entire DMP business depends on an organization enjoying recognition of tax exempt status under §501(c)(3) .

**Private Benefit**

XXX was formed for the private benefit of XXX and his solely owned related for-profit entities. Once a client was enrolled in a DMP, all of the processing had been planned to be turned over to XXXXX, for back office processing and customer services. XXX did not seriously solicit any companies other than XXXXX to process its DMPs. XXXXX also was responsible for all of XXX's advertising and marketing activities. XXX licensed his Interactive Counseling Tool software through XXXXX to XXX. Another for-profit entity of XXX, XXXXX, provided communication services to XXXXX. XXX maintained complete control over XXX and XXXXX.

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Although the Service does not allege that excess payments were made to XXXXX, XXX benefited substantially from the arrangement as it was a captive contract where no outsiders were permitted to bid or otherwise compete for the service agreements and the arrangement provided for a livelihood for XXX that he could not otherwise enjoy without the participation of XXX. XXX, in effect, acted as a debt collection service for the creditors. See Christian Stewardship Assistance, Inc. v. Commissioner, American Campaign Academy v. Commissioner, and Retired Teachers Legal Fund v. Commissioner.

The Interactive Counseling Tool software program was utilized by XXX in constructing and managing its DMP program. The program only had value to a bona fide §501(c)(3) entity that could lawfully engage in debt counseling services, hence XXX formed XXX. Utilizing XXX in this fashion contributes to his private benefit. See est of Hawaii v. Commissioner and International Post Graduate Foundation v. Commissioner.

**CONCLUSION:**

The Service conducted an examination of XXX's activities for the tax year ending December 31, XXXX. As a result of the examination, the Service proposes the revocation of XXXXX exemption status under IRC §501(c)(3), because XXX is not operated exclusively for exempt purposes and has provided an private benefits to select individuals.